DEPARTMENT OF STATE REVENUE
LETTER OF FINDINGS NUMBER: 02-0349
CORPORATE INCOME TAX
For Years 1996-1999

NOTICE: Under Ind. Code § 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUES

I. **Gross Income Tax –** Out-of-state sales

Authority: IC 6-2.1-2-2; IC 6-2.1-2-3; IC 6-2.1-2-4; IC 6-2.1-2-5; IC 6-2.1-3-3; 45 IAC 1.1-3-3(c).

Taxpayer protests the imposition of gross income tax on sales made to out-of-state customers.

STATEMENT OF FACTS

Taxpayer is a corporation that is wholly owned by a corporate Parent in California. Taxpayer holds certain manufacturing and operating assets and properties. Taxpayer manufactures metal containers and component parts, as well as metal caps and closures, for Parent and other unrelated third parties. Taxpayer does all of its manufacturing at four plants—all of which are located in Indiana.

When the manufacturing process is complete, Taxpayer stores its finished products either at its own plant or at a third-party warehouse until Taxpayer is instructed by its customer—in this case, Parent—to drop ship its goods to the end purchaser—in this case—Parent's customers. Taxpayer contracts with common carriers for delivery of its goods. Prior to the shipment, Taxpayer prepares invoices and corresponding bills of lading for the product being shipped. Taxpayer prepares this paperwork at the plant location from which the goods are shipped. Taxpayer prints these invoices on generic invoices. These invoices instruct the end purchaser to remit payment to Parent directly.

Taxpayer drop ships its products to purchasers in numerous states. During the audit period, approximately 2 percent of the products were shipped to purchasers in Indiana. When Parent's customers receive the product, the customers have the right to accept or reject the shipment. Until a shipment is accepted, Taxpayer retains the legal title to—and bears the risk of loss for—the products. When a purchaser accepts a shipment, the title for those products passes from Taxpayer to Parent, and then from Parent to its customer, the end purchaser. Each of these transactions occurs at the location of the end purchaser where the shipment is accepted.

Legal title, possession, and risk of loss and damage remain with Taxpayer until the goods are both received by and accepted by Parent's customers. Pursuant to an agreement between Taxpayer and Parent, Parent is obligated to compensate Taxpayer, on a monthly basis, at a contractually negotiated price for products and delivery costs. Parent's obligation to Taxpayer occurs only after Parent's customers have received and duly accepted the shipped goods.

Under the agreement, Parent is required to compensate Taxpayer for Parent's purchases—regardless of when Parent receives payment from its customers. Generic invoices sent with the shipments to Parent's customers require that payment for the goods be sent directly to Parent.

In general, Parent's customers deal directly with Parent. These end purchasers also deal directly with Taxpayer on certain issues, such as production schedule changes, product delivery, and product warranty, If, after receiving and accepting the shipment of goods, Parent's customer becomes dissatisfied with the product and reject the goods, Taxpayer is required to indemnify Parent for those rejected goods. Specifically, Taxpayer agrees to warrant that all goods produced for Parent are produced in conformity with Parent's specifications; Taxpayer warranties to Parent that all goods it produces for Parent will meet or exceed Parent's product warranties to its customers. Taxpayer is obligated under the agreement to indemnify Parent for any breach of those customer warranties.

I. **Gross Income Tax** **–** Out-of-state sales

DISCUSSION

IC 6-2.1-2-2(a)(1) imposes a gross income tax on the entire taxable gross income of a taxpayer who is a resident or a domiciliary of Indiana. The gross income tax also is imposed on a non-resident taxpayer who receives gross income derived from activities or businesses or any other sources within Indiana. IC 6-2.1-2-2(a)(2). The gross income tax is imposed at two rates, the high rate of 1.2 percent and the low rate of 0.3 percent. IC 6-2.1-2-3. The rate of tax is determined by the type of transaction from which the taxable gross income is received. IC 6-2.1-2-2(b). The receipts from wholesale sales and from selling at retail are taxed at the low rate. IC 6-2.1-2-4. Receipts from service activities and certain other business activities are taxed at the high rate. IC 6-2.1-2-5.

Gross income derived from business conducted in interstate commerce is exempt from the gross income tax to the extent such taxation is prohibited by the United States Constitution. IC 6-2.1-3-3. Gross income derived from the sale of tangible personal property in interstate commerce is not subject to the gross income tax if the sale is not completed in Indiana. 45 IAC 1.1-3-3(c).

Taxpayer asserts that its sales delivered out-of-state to Parent's non-Indiana customers are part of interstate commerce and as such are not subject to gross income tax. The Department concurs on the basis that these sales are completed when delivered to the customer.

FINDINGS

Taxpayer's protest is sustained.

AG/JM/DK 051612